



UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D.C. 20548

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PROCUREMENT, LOGISTICS,  
AND READINESS DIVISION

B-205720

MARCH 8, 1982

The Honorable Caspar W. Weinberger  
The Secretary of Defense



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Attention: Director, GAO Affairs

Dear Mr. Secretary:

Subject: Reporting Competition in Defense Procurements—  
Recent Changes Are Misleading (PLRD-82-45)

Determining the real extent of competition in Department of Defense (DOD) procurements is becoming increasingly difficult. In the past, DOD experienced declines in competitive procurements that caused increased congressional concern. Amid congressional inquiries about the extent of competition, DOD officials portrayed competitive rates for the first half of fiscal year 1981, ranging from a high of 69 percent in testimony before the Senate Committee on Armed Services to a low of 45 percent in their procurement statistics.

DOD procurement statistics were also revised to include certain highly competitive nonmilitary awards and to exclude certain noncompetitive military awards. In our opinion, DOD's presentation of, and changes to, its statistics could decrease the credibility of the statistics and could even lead to a real decline in competition. Furthermore, we realize DOD has undertaken management initiatives to increase competition and are concerned that changes in reporting competitive and noncompetitive statistics will distort the historical base and make it difficult to measure improvements in competitive buying.

OBJECTIVES, SCOPE, AND METHODOLOGY

This review was undertaken because of ongoing congressional concern about competition and because of the lack of consistency in reported amounts of competitive DOD contracts.

We reviewed the various reports on DOD competitive contracts to determine where differences occurred. We isolated recent changes to evaluate their impact on reported competition and discussed the rationale for these changes with DOD officials.

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INTERPRETATIONS AND CHANGES CAUSE  
CONFUSION OVER COMPETITIVE STATISTICS

Considerable liberty has been taken in the presentation of competition in DOD procurement. During testimony, three procurement categories classified by DOD as noncompetitive were presented as competitive. This shifted \$9.5 billion from DOD's noncompetitive to its competitive procurements.

The Congressional Record of June 24, 1981 (p. H 3292), reported that competition in DOD procurement in the first half of fiscal year 1981 had reached 69 percent of total procurement. DOD officials, likewise, testified before the Senate Committee on Armed Services on July 28, 1981, that 69 percent of DOD purchases were competitive in the first half of fiscal year 1981 when DOD's statistics indicated 45 percent were competitive.

In addition, two revisions have been made that alter the way the statistics are compiled. First, certain noncompetitive categories of procurement have been excluded from DOD procurement reports. This has deleted over \$3.3 billion from DOD's previously reported noncompetitive procurements. Second, for the first time, civil works programs have been included in DOD procurement reports. This has added over \$1.5 billion to reported competition. These two revisions inflated DOD's competition to the reported 45 percent. Our analysis shows that, when using DOD's historical statistical classifications, competition in the first half of fiscal year 1981 was 41 percent. The table on the following page shows the impact of DOD's actions versus historical statistical classifications for the first half of fiscal year 1981.

DOD Procurement in First Half of Fiscal Year 1981

	<u>Historical statistical classifications</u>	<u>Revised statistical classifications</u>	<u>Revised statistical classifications with altered presentation</u>
	----- (percent) -----		
<u>Competitive</u>			
Formal advertising	5.8	7.6	7.6
Price negotiated	<u>25.4</u>	<u>27.5</u>	<u>27.5</u>
Total price	31.2	35.1	35.1
Design	<u>9.5</u>	<u>10.1</u>	<u>10.1</u>
Total price and design	<u>40.7</u>	<u>45.2</u>	<u>45.2</u>
Follow-on after price	-	-	1.6
Follow-on after design	-	-	19.0
Catalog or market	<u>-</u>	<u>-</u>	<u>2.8</u>
Total competitive	<u>40.7</u>	a/ <u>45.2</u>	a/ <u>68.6</u>
<u>Noncompetitive</u>			
Follow-on after price	1.5	1.6	-
Follow-on after design	17.9	19.0	-
Catalog or market	2.7	2.8	-
Other noncompetitive	<u>37.2</u>	<u>31.3</u>	<u>31.3</u>
Total noncompetitive	<u>59.3</u>	a/ <u>57.7</u>	a/ <u>31.3</u>

a/Does not add due to rounding.

The new classifications, as discussed below, could mislead the Congress and the public by inflating the competitive statistics and could result in relaxing the pressures to obtain greater competition.

INTERPRETATIONS CAUSE CONFUSION

Three categories designated noncompetitive were presented in testimony as competitive. These include

--follow-on contracts where the original award was based on price competition,

--follow-on contracts where the original award was based on design competition, and

--sole-source contracts to a contractor at a catalog or market price for commodities sold in substantial quantities to the public.

By presenting these contracts as competitive, DOD increased the competitive/noncompetitive ratio by 24 percent.

In our opinion, the assumption that follow-ons should be considered competitive if the original award is competitive is questionable and can contribute to a decline in competition. DOD uses the classification "follow-on" to identify certain noncompetitive contracts where a previous award, made competitively, creates a situation which necessitates that subsequent contracts be awarded to the same contractor. We believe that being tied to one contractor when many exist is no more indicative of a competitive procurement than a situation where there is only one vendor. Classifying follow-on contracts as competitive eliminates any distinction between subsequent noncompetitive and competitive awards. This could remove the incentive for procurement officers to compete these procurements wherever feasible and thereby contribute to a decline in competition.

We recognize that some noncompetitive follow-ons for procurements, such as major weapon systems, are inevitable. However, when such contracts cannot be competed for sound reasons, we suggest that they be classified "Noncompetition--No Potential," as discussed below.

As in the case of follow-ons, the assumption that catalog or market price contracts assure the Government the best competitive price is open to question. While the market in certain instances may set prices through competition, other forms of market pricing involve monopolies, oligopolies, and cartels where prices are not established through competition. For example, the actions of the OPEC Oil Cartel were highly publicized as attempts to control the supply and prices of oil. In the first half of fiscal year 1981, noncompetitive procurements of petroleum products accounted for over 85 percent of the dollar expenditures in the catalog/market price category. In addition, we believe classifying catalog or market price contracts as competitive may contribute to a decline in competition if contracting officers believe they do not have to obtain competition on items that may be justified as catalog or market price.

#### CHANGES MADE TO STATISTICS

Certain noncompetitive procurement categories were excluded from the procurement data base. These categories include contracts which were awarded

- for brand name items for commissary resale,
- to educational and nonprofit institutions,

- to monopolies for utilities where the price negotiated is based on rates set by law or regulation, and
- to minority contractors pursuant to section 8(a) of the Small Business Act (15 U.S.C. 637 (a)).

DOD has excluded these contracts from the statistical base because it believes they are not susceptible to competition. The main problem with this change is that it incorrectly implies that there is no opportunity to obtain competition on any of these procurements. For example, while the contracts to educational institutions are predominantly noncompetitive, more than \$25 million in competitive awards were made to educational institutions in fiscal year 1979. If the extent of competition for contracts to educational institutions is no longer reported, contracting officers and program officials may no longer be encouraged to obtain competition where it is available and useful. This could result in a decline in competition.

The following table shows the enhancement of the competitive/noncompetitive ratio resulting simply from excluding noncompetitive contracts.

Effect of Excluding Certain Non-Competitive Contracts from the Data Base in First Half of Fiscal Year 1981

	<u>Former practice includes these contracts</u>	<u>Effect of excluding these contracts</u>
----- (percent) -----		
<u>Competitive</u>		
Formal advertising	7.1	7.6
Price	25.4	27.5
Design	<u>9.4</u>	<u>10.1</u>
Total competitive	<u>41.9</u>	<u>45.2</u>
<u>Noncompetitive</u>		
Follow-on price	1.5	1.6
Follow-on design	17.5	19.0
Catalog or market	2.6	2.8
Other noncompetitive	<u>36.6</u>	<u>31.3</u>
Total noncompetitive	<u>58.2</u>	<u>54.7</u>

As can be seen from the table, excluding certain noncompetitive contracts simply creates the illusion of improving competition.

When there is only one contractor available, we suggest including the contract in the statistics but using the classification "Noncompetitive--No Potential."

In 1980 DOD began including in its competitive statistics 1/ nonmilitary contracts for the civilian functions 2/ of the Army Corps of Engineers. It is our understanding that these contracts are not funded through DOD appropriations, nor are they awarded through regular DOD procurement offices. Instead, these contracts are funded directly to the civilian function, as authorized under the Rivers and Harbors Act, and are awarded through the civilian function's procurement office.

Contracts for civilian functions are highly competitive. For example, in fiscal year 1980, 86 percent of the contracts for civil functions were competitive, equal to \$1.5 billion of competitive awards. In the first half of fiscal year 1981, competition on these contracts reached 89 percent. A comparison of fiscal year 1981 competitive statistics, including and excluding contracts for the civil functions, demonstrates the impact of including these contracts for the first time in DOD's statistics.

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1/Concurrent with the inclusion of contracts for civil functions, DOD changed the title of its statistical report from "Military Prime Contract Awards" in fiscal 1979 to "Prime Contract Awards" in fiscal 1980, acknowledging the fact that the statistics no longer reflect only military awards.

2/Includes among other programs, the Civil Works Program which involves major dams, locks, levees, and other structures.

Effect of Including Civil Functions  
on Extent of Competition in  
First Half of Fiscal Year 1981

<u>Competitive</u>	<u>Civil functions only</u>	<u>DOD including civil functions</u>	<u>DOD excluding civil functions</u>
	----- (percent) -----		
Formal advertising	63.8	7.6	6.3
Price	23.4	27.5	27.6
Design	<u>1.6</u>	<u>10.1</u>	<u>10.3</u>
 Total competitive	 <u>a/88.8</u>	 <u>a/45.2</u>	 <u>a/44.2</u>
 <u>Noncompetitive</u>			
Follow-on price	0.2	1.6	1.6
Follow-on design	0.1	19.0	19.4
Catalog or market	-	2.8	2.9
Other noncompetitive	<u>10.8</u>	<u>31.3</u>	<u>31.8</u>
 Total non- competitive	 <u>a/11.1</u>	 <u>a/54.7</u>	 <u>a/55.7</u>

a/Does not add due to rounding.

By including contracts for civil functions, DOD reported an increase in formal advertising from 6.3 percent to 7.6 percent during the first half of 1981 and an overall increase in competition of 1 percent during this period. If such contracts are to be included in the future, we believe there should be a reconciliation with past data to show the year-to-year trend for the totals with and without civil functions.

DOD BELIEVES SOME CHANGE IS NEEDED  
TO BETTER PRESENT COMPETITION

It appears that DOD's recent changes in the presentation of its procurement statistics is an attempt to highlight areas where there is no potential to obtain competition. According to DOD officials, DOD's historical reporting of competition does not adequately present this data. They believe that a significant portion of DOD's procurements have no competitive potential. While we agree that it is impractical to obtain competition on many contracts, we do not believe, for the reasons discussed above, that DOD's recent changes to reporting competition are appropriate without further adjustment. In our opinion, a better way to identify contracts with no competitive potential would be to break down the noncompetitive category into "Noncompetitive--Potential" and "Noncompetitive--No Potential."

Noncompetitive--potential

Many of the types of contracts awarded noncompetitively offer the potential for competition. For example, contracts awarded under section 8A of the Small Business Act may have competitive potential, but because they are intended to assist disadvantaged businesses they are not competed. Such contracts could be displayed under a "Noncompetitive--Potential" subcategory without distorting DOD's statistics or weakening DOD's incentive to obtain competition.

This subcategory would include contracts which are awarded

--pursuant to section 8A of the Small Business Act;

--under extenuating circumstances, such as time constraints or to maintain an industrial base; and

--in the absence of a data package sufficient to obtain competition.

Noncompetitive--no potential

Similarly, many of the types of contracts awarded noncompetitively offer no potential for competition. These contracts could be displayed under a "Noncompetitive--No Potential" subcategory without distorting statistics. This subcategory would include:

--Follow-on contracts to a weapon producer who is locked in by extensive investment in plans and facilities or similar circumstances which make it impracticable to obtain competition. The impracticability of obtaining competition, however, should be fully supportable.

--Contracts to vendors who are the only source.

--Other contracts, such as certain utilities, where the price is set by law or regulation.

With these new subcategories, DOD could then better identify areas where there is no potential to obtain competition without distorting historical trends or discouraging competition.

CONCLUSIONS

In our opinion, the fact that DOD is obtaining 41 percent of the procurement dollars in competitive contracts, based on past statistical classifications, should not be considered either favorable or unfavorable. To properly evaluate DOD's efforts to obtain competition, procurements must be put into the context of what levels of competition are possible.

AGENCY COMMENTS AND OUR EVALUATION

DOD officials concurred with our conclusion that follow-on and catalog or market price contracts are noncompetitive. They emphasized that these contracts are reported as noncompetitive and that DOD officials' portrayal of these categories "as based on competition" was not intended to realine the statistics but rather to distinguish them from other noncompetitive contracts. They disagreed with the report's conclusions that certain noncompetitive contracts should remain in the data base and that other nonmilitary contracts should not have been included in the data base.

Regarding the removal of contracts for utilities, brand name items for commissary resale, services from educational and non-profit institutions, and goods or services from minority contractors under the 8A program, DOD believes that no opportunity exists for competition in these areas and therefore these contracts should be removed from the data base. In addition, the inclusion of nonmilitary contracts for the civilian functions of the Army Corps of Engineers was based on the fact that such contracts are awarded by the Corps of Engineers' personnel under the Defense Acquisition Regulation.

We believe DOD's position that contracts should be removed from the data base because they offer no opportunity for competition is inconsistent with the reporting of whether competition was or was not obtained. This position also incorrectly implies that all of the noncompetitive contracts left in the data base had the opportunity to get competition. Furthermore, removing contracts from the data base because they do not offer the potential for competition will ultimately remove many procurements for major weapon systems and result in a highly competitive data base which represents only a fraction of the annual contracts awarded.

We also believe DOD's position that nonmilitary contracts be included if they involve military personnel and the Defense Acquisition Regulation will distort the data base. The intention of the statistics is to portray DOD expenditures. Consequently, by including nonmilitary contracts, the focus on examining the extent of competition on military awards is lost.

We believe the annual Prime Contract Awards publication is the primary source of information for DOD procurements. It is therefore imperative that these statistics contain all of the prime contracts DOD awards and be limited to only military procurements.

DOD disagreed with our recommendation to maintain the historical presentation of its statistics. It believes that while frequent changes to the reporting of competition would be unwise, the principle of consistency should not preclude warranted changes.

Additionally, DOD believes our recommendation to further break down the noncompetitive category would not satisfy its objective of a better presentation of the data.

We support warranted changes and suggest procedures in our report that will allow DOD to portray contracts where competition is not feasible without distorting the data base. We want to emphasize that we are not opposed to changes that will improve the understanding of the statistics. However, we believe changes similar to those recently implemented by DOD can only lead to confusion.

RECOMMENDATIONS

We recommend that the Secretary of Defense:

- Maintain longstanding historical classifications of military procurement contract data for purposes of displaying competitive versus noncompetitive trends.
- Include in the noncompetitive category, new subcategories entitled "Noncompetitive--No Potential" and "Noncompetitive--Potential," as described above.
- Show procurements for civilian functions as an additional calculation after displaying the traditional and historical statistical classifications.

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As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House Committee on Government Operations and the Senate Committee on Governmental Affairs not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report. We are sending copies of this report to the Chairmen, Senate and House Committees on Armed Services and on Small Business.

Sincerely yours,



Donald J. Horan  
Director